

# *VIEWS FROM DR. DAVE*

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Road Warrior of Agriculture: [www.cornandsoybeandigest.com](http://www.cornandsoybeandigest.com)

Ag Globe Trotter: [www.northwestfcs.com](http://www.northwestfcs.com)

# *Producer & Portfolio Shock Test (1)*

- cash flow & profits
  - 10% decrease in revenue
  - 10% increase in expenses
  - 3% increase on variable rates
- liquidity- top ten issues
  - concentration of assets
  - inventory price protected
  - inventory quality & contract quality
  - account receivable concentration
  - account receivable quality
  - prepaid expense cycle
  - unsecured creditor
  - crops in field – crop insurance
  - cash
  - accounts payable-deferred taxes

# *Producer & Portfolio Shock Test (2)*

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- land & asset values
  - 10-25-40 percent decline
  - deferred taxes
  - asset quality
- concentration, interconnectedness, third party
  - contracts
  - percentage
  - scenario testing

# *Dr. Dave's Key Perspectives in Agricultural Credit*

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- family living withdrawals
- growth
  - financial
  - business systems
  - business acumen
- volatility- working capital management
- debt efficiency- total debt/EBITDA
- widening gap of farm profitability

# *Trends in Lending Observed From the Road*

- from scorecard lending to relationship lending
- hot money & hot credit institutions
- alignment with talent-customers, agribusinesses & lenders
- regulatory overreaction
- young producer & women lending strategy
- producer lifelong learning & knowledge centers
- culture & people alignment
- 6 year rule /15 year rule
- criteria for endurance in a super cycle/land correction
  - profits
  - cash flow
  - liquidity
  - efficiency
  - scenario & shock testing
- evolution & transition

## Strategic Business Performance Index

Variable	Criteria	Year:	X	Y	Z	Projected	Worst Case	Best Case
<b>Profitability</b>								
<b>Return on Assets</b>			<b>8.3%</b>	<b>10.0%</b>	<b>12.2%</b>	<b>12.7%</b>	<b>3.1%</b>	<b>18.7%</b>
	Rating		Index	Index	Index	Index	Index	Index
	more than 10 percent	4	<b>3</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>2</b>	<b>4</b>
	6 - 10 percent	3						
	2 - 5 percent	2						
	0 - 1 percent	1						
	less than 0 percent	0						
<b>Financial Efficiency</b>								
<b>Operating Efficiency</b>			<b>25.0%</b>	<b>24.3%</b>	<b>27.5%</b>	<b>37.2%</b>	<b>20.9%</b>	<b>44.4%</b>
	Rating		Index	Index	Index	Index	Index	Index
	more than 35 percent	4	<b>3</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>2</b>	<b>4</b>
	25 - 35 percent	3						
	15 - 24 percent	2						
	0 - 14 percent	1						
	less than 0 percent	0						
<b>Capital Efficiency</b>								
<b>Asset Turnover</b>			<b>64.1%</b>	<b>75.6%</b>	<b>72.6%</b>	<b>46.3%</b>	<b>36.8%</b>	<b>52.3%</b>
	Rating		Index	Index	Index	Index	Index	Index
	more than 70 percent	4	<b>3</b>	<b>4</b>	<b>4</b>	<b>1</b>	<b>0</b>	<b>2</b>
	60 - 69 percent	3						
	50 - 59 percent	2						
	40 - 49 percent	1						
	less than 40 percent	0						
<b>Debt Efficiency</b>								
<b>Total Debt/EBITDA</b>			<b>4.36%</b>	<b>3.41%</b>	<b>2.44%</b>	<b>3.74%</b>	<b>8.40%</b>	<b>2.77%</b>
	Rating		Index	Index	Index	Index	Index	Index
	less than 2.0	4	<b>2</b>	<b>3</b>	<b>3</b>	<b>3</b>	<b>0</b>	<b>3</b>
	2.0 - 3.9	3						
	4.0 - 5.9	2						
	6.0 - 8.0	1						
	more than 8.0	0						
<b>Liquidity</b>								
<b>Working Capital Sufficiency</b>			<b>8.6%</b>	<b>7.8%</b>	<b>12.4%</b>	<b>6.8%</b>	<b>8.5%</b>	<b>6.0%</b>
	Rating		Index	Index	Index	Index	Index	Index
	more than 50 percent	4	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
	40 - 49 percent	3						
	30 - 39 percent	2						
	20 - 29 percent	1						
	less than 20 percent	0						
<b>Solvency</b>								
<b>Percent Equity Ratio</b>			<b>28.6%</b>	<b>37.3%</b>	<b>51.4%</b>	<b>35.5%</b>	<b>35.5%</b>	<b>35.5%</b>
	Rating		Index	Index	Index	Index	Index	Index
	more than 75 percent	4	<b>1</b>	<b>1</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>1</b>
	61 - 75 percent	3						
	40 - 60 percent	2						
	25 - 39 percent	1						
	less than 25 percent	0						
<b>Repayment Ability</b>								
<b>Term Debt Coverage Ratio</b>			<b>146.7%</b>	<b>170.9%</b>	<b>176.0%</b>	<b>157.3%</b>	<b>49.6%</b>	<b>225.1%</b>
	Rating		Index	Index	Index	Index	Index	Index
	more than 200 percent	4	<b>2</b>	<b>3</b>	<b>3</b>	<b>3</b>	<b>0</b>	<b>4</b>
	150 - 199 percent	3						
	125 - 149 percent	2						
	100 - 124 percent	1						
	less than 100 percent	0						
<b>FINANCIAL INDEX</b>			<b>14</b>	<b>17</b>	<b>19</b>	<b>16</b>	<b>5</b>	<b>18</b>

## Strategic Business Performance Index, Continued

Variable	Criteria	Year:	X	Y	Z	Projected	Worst Case	Best Case
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### Management (Sixth C: Cranium)

1 point for each Action



		Index	Index	Index	Index	Index	Index
Enterprise Cost of Production	1	1	1	1	1	1	1
Written Marketing Plan	1	1	1	1	1	1	1
Written Business Plan Utilized	1	0	0	0	0	0	0
Execution of Goals	1	1	1	1	1	1	1
Management Succession Plan	1	0	0	0	0	0	0
Advisor Team & Use	1	1	1	1	1	1	1
Risk Management Plan	1	0.5	0.5	0.5	0.5	0.5	0.5
Training programs for Management & Employees	1	0	0	0	0	0	0
Environmental/ Conservation Management Plan	1	1	1	1	1	1	1
Long Term Written Lease Arrangements or Ownership of 75%+ of Land/Assets	1	0	0	0	1	1	1
<b>MANAGEMENT INDEX</b>		<b>5.5</b>	<b>5.5</b>	<b>5.5</b>	<b>6.5</b>	<b>6.5</b>	<b>6.5</b>

### Credit History

FICO & Beacon Scores

		Index	Index	Index	Index	Index	Index
> 800	8	<b>4</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>4</b>
750 to 799	6						
700 to 749	5						
650 to 699	4						
600 to 649	3						
500 to 599	2						
450 to 499	-1						
< 450	-5						
<b>CREDIT INDEX</b>		<b>4</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>4</b>	<b>4</b>
<b>Total of All Indexes</b>		<b>23.5</b>	<b>26.5</b>	<b>28.5</b>	<b>26.5</b>	<b>15.5</b>	<b>28.5</b>
<b>PERFORMANCE LEVEL</b>		<b>4</b>	<b>4</b>	<b>3</b>	<b>4</b>	<b>3</b>	<b>5</b>

<u>Level</u>	<u>Index</u>	<u>Description</u>
Level 1	40 or higher	Exceptional Performance
Level 2	34 to 39	Excellent Performance
Level 3	28 to 33	Good Performance
Level 4	22 to 27	Average Performance - Improve Management Actions
Level 5	21 or less	Under Performing - Substantial Change Needed in Management Actions

Developed by: David M. Kohl, Ph.D. & Scott A. Mickey

## Composite Credit Index for Commercial Agriculture

Variable	Criteria	Year X	Year Y	Year Z	Proj.	Worst	Best
<b>Repayment Ability</b>							
<b>Term Debt and Lease Coverage Ratio</b>		Index	Index	Index	Index	Index	Index
	more than 200 percent	4	4	4	4	4	4
	150 - 199 percent	3	3	3	3	3	3
	125 - 149 percent	2	2	2	2	2	2
	100 - 124 percent	1	1	1	1	1	1
less than 100 percent	0	0	0	0	0	0	
<b>Liquidity</b>							
<b>Working Capital / Total Revenue</b>		Index	Index	Index	Index	Index	Index
	more than 25 percent	4	4	4	4	4	4
	16 - 25 percent	3	3	3	3	3	3
	11 - 15 percent	2	2	2	2	2	2
	0 - 10 percent	1	1	1	1	1	1
negative	0	0	0	0	0	0	
<b>Solvency</b>							
<b>Debt-to-Asset Ratio</b>		Index	Index	Index	Index	Index	Index
	less than 25 percent	4	4	4	4	4	4
	25 - 39 percent	3	3	3	3	3	3
	40 - 60 percent	2	2	2	2	2	2
	61 - 75 percent	1	1	1	1	1	1
more than 75 percent	0	0	0	0	0	0	
<b>Debt Servicing Efficiency</b>							
<b>Total Debt / EBITDA</b>		Index	Index	Index	Index	Index	Index
	less than 3.0	4	4	4	4	4	4
	3.0 - 4.5	3	3	3	3	3	3
	4.6 - 6.0	2	2	2	2	2	2
	6.1 - 7.5	1	1	1	1	1	1
more than 7.5	0	0	0	0	0	0	
<b>Profitability</b>							
<b>Return on Assets Ratio</b>		Index	Index	Index	Index	Index	Index
	more than 10 percent	4	4	4	4	4	4
	6 - 10 percent	3	3	3	3	3	3
	2 - 5 percent	2	2	2	2	2	2
	0 - 1 percent	1	1	1	1	1	1
less than 0 percent	0	0	0	0	0	0	
<b>Financial Efficiency</b>							
<b>Operating Expense / Revenue Ratio (excluding interest &amp; depreciation)</b>		Index	Index	Index	Index	Index	Index
	less than 65 percent	4	4	4	4	4	4
	65 - 74 percent	3	3	3	3	3	3
	75 - 85 percent	2	2	2	2	2	2
	86 - 100 percent	1	1	1	1	1	1
more than 100 percent	0	0	0	0	0	0	
<b>Credit History</b>							
<b>FICO &amp; Beacon Scores</b>		Index	Index	Index	Index	Index	Index
	greater than 800	8	8	8	8	8	8
	750-800	6	6	6	6	6	6
	700-749	5	5	5	5	5	5
	650-699	4	4	4	4	4	4
	600-649	3	3	3	3	3	3
	500-599	2	2	2	2	2	2
450-499	-1	-1	-1	-1	-1	-1	
less than 450	-5	-5	-5	-5	-5	-5	
<b>Total of All Indexes</b>		<b>17</b>	<b>18</b>	<b>22</b>	<b>20</b>	<b>10</b>	<b>22</b>

Level	Index	Description
Level 1	29 - 32	This loan is very serviceable and would require minimal supervision and quality for best rates.
Level 2	20 - 28	This loan is serviceable and would require covenants, supervision, and second tier rates.
Level 3	12 - 19	This loan is questionable: if made, strict covenants, close supervision and rates that reflect risk.
Level 4	< 10	Reject; if you have one, it may require workout.

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